

# Questions and Answers

## On

### Pre-tax Voluntary Contributions

(Updated 10-31-2003)

#### 1) What does the 2003 IRS ruling change?

The new IRS ruling adds the possibility of making additional Annuity Savings Account (ASA) contributions with pre-tax dollars. This option will be available for qualifying members. (See below for more details on how members will qualify to make these contributions.) Qualifying members must select whether to make their additional ASA contributions with post-tax dollars or pre-tax dollars. However, some very important limitations apply. For example, as a condition of the ruling an election to make pre-tax contributions may not be changed until the member retires or goes to work for a different employer. The IRS requires that the election be "irrevocable." See more details about the terms and conditions of the election below.

#### 2) Who is qualified to make pre-tax contributions?

Qualified members are those who are currently working for an employer that is participating in the pre-tax program, and who are within their two-year election window. An election window begins on September 1 after the end of the plan year (June 30) in which a member earns or is re-credited with five years of service. More information about the election window is described below.

#### 3) When is my election window to make a pre-tax election?

Under the terms of the IRS ruling, to receive a two-year election window, you must (i) have earned five years of PERF or TRF service in the prior plan year (ending June 30), and (ii) currently work for an employer who is participating in the pre-tax program. Your election window is the period of time when you will be able to elect to make pre-tax contributions. The two-year window starts on the September 1 following the plan year in which you earned five years of service.

Members who have changed jobs may also be entitled to have a two-year election window. As of June 30, PERF and TRF will determine who has completed or was re-credited with five years of service in the prior calendar year. Beginning on September 1, those members will receive a two-year election window. (See below for more information on being "re-credited" with five years of service after leaving PERF or TRF covered employment.)

Example 1: John participates in PERF and completed five years of PERF service in the month of March 2005. John's employer has adopted a resolution to participate in the pre-tax voluntary contribution program. Based on PERF's June 30, 2005 records, John completed five years of service credit in the plan year between July 1, 2004 and June 30, 2005. Therefore John is eligible to participate in the pre-tax voluntary contribution program and his two-year election window begins on September 1, 2005. (Note: the same timing rules apply to both PERF and TRF. If John were a TRF member, the same rule would apply).

Example 2: Alice participates in PERF and completed five years of PERF service in August 2005. Alice's employer has adopted a resolution to participate in the pre-tax voluntary contribution program. PERF determines who is eligible for the two-year election window that begins in September 2005 based on its June 30, 2005 records. Because Alice did not have five years of service as of June 30, 2005, she is not eligible to make pre-tax contribution election in September, 2005. However, as of June 30, 2006, PERF records will show her as having earned five years of credit between July 1, 2005 and June 30, 2006. Therefore, her two-year election window begins on September 1, 2006. (Note: the same timing rules apply to both PERF and TRF. If Alice were a TRF member, the same rule would apply).

**4) Is there a special election window for when this program starts in 2003?**

Yes. Anyone who has at least five years of creditable PERF or TRF service as of June 30, 2003, will be entitled to a two-year election window starting on September 1, 2003 if their employer opts into this program. You may not make an election until your employer adopts this program, and (even if your employer completes their adoption earlier) you may not make your election until September 1, 2003. For years thereafter, only members who complete their fifth year of service in a plan year ending June 30 will have a two-year election window beginning on the following September 1.

**5) Please explain again my election window and how it relates to when my employer adopts their resolution.**

**2003 Plan Year**

|   |   |
|---|---|
| If your employer adopted the resolution | 07/01/2003 thru 12/31/2003  |
| If you                                  | Have 5 years of PERF/TRF service or more as of 06/30/2003               |
| Your Election Window is                 | The later of 09/01/2003 or the employer's adoption date thru 08/31/2005 |

**2004 Plan Year**

|   |   |
|---|---|
| If your employer adopted the resolution | 01/01/2004 thru 08/31/2004                        |
| If you                                  | Have 5 years of PERF/TRF service as of 06/30/2004 |
| Your Election Window is                 | 09/01/2004 thru 08/31/2006                        |

## **2005 Plan Year**

|   |   |
|---|---|
| If your employer adopted the resolution | 09/01/2004 thru 08/31/2005                        |
| If you                                  | Have 5 years of PERF/TRF service as of 06/30/2005 |
| Your Election Window is                 | 09/01/2005 thru 08/31/2007                        |

### **6) What does my employer have to do before I may make a pre-tax election?**

Your employer must elect to participate in the pre-tax program by adopting a resolution with standard IRS-language. If your employer does not elect to participate by adopting this resolution, you may not make voluntary contributions on a pre-tax basis.

### **7) When can I make the pre-tax election?**

You may make a pre-tax election at any time during your two-year election window.

### **8) What happens if I do not elect to participate during my two-year election window? Can I choose to participate at a later date?**

You may only elect to participate in the pre-tax contribution program during your election window. If you do not elect to participate during the two-year election window that occurs after you earn five years of service, you cannot later choose to participate unless you leave your current employment and begin a PERF or TRF covered job with a different employer.

### **9) How do I make the pre-tax election?**

You may make a pre-tax election by completing the election form during your election window. Important: Remember that you cannot change your pre-tax election. It is binding and irrevocable. See more details below.

### **10) Can I make a post-tax election in addition to a pre-tax election?**

Yes. You can make a post-tax election at the same time you make a pre-tax election, or at a later date, but the total of your pre-tax and post-tax voluntary contributions cannot exceed 10% of your compensation.

### **11) How long will the pre-tax election apply?**

YOUR PRE-TAX ELECTION CANNOT BE CHANGED. IT WILL CONTINUE TO APPLY AS LONG AS YOU WORK FOR THE SAME EMPLOYER, EVEN IF YOU LEAVE AND COME BACK TO WORK WITH THAT EMPLOYER.

### **12) What if I leave and return to work?**

If you leave work and return to the same employer, your pre-tax election will continue in force.

If you leave work and then take a job with a different employer and have not taken a refund of your ASA, you will have a new election window beginning on the following September 1.

Example 3: Assume that John, described in Example 1, made a pre-tax election during the two-year window that began after his fifth year of service. After working for a few years and making pre-tax contributions, he leaves PERF employment to work for a private company that does not participate in PERF. After working in the private sector for a few years, he returned to work in a PERF-covered position. If John returns to work for the same PERF employer that he worked for before leaving for the private sector, his pre-tax election will immediately apply to his salary when he resumes work.

Example 4: If John returns to work in a PERF-covered position for a new PERF employer, he will receive a new two-year election window. If John took a refund, John is re-credited with his prior service six months after starting with his new employer. The two-year election window is determined in the same manner as for someone who completes five years of service for the first time: as of June 30, PERF and TRF will determine who completed or was re-credited with five years of service in the prior plan year. Beginning on September 1, those members will receive a two-year election window.

### **13) If I make a pre-tax election, can my election be changed or stopped?**

While you continue in employment with your employer, you cannot increase, decrease, or otherwise change your pre-tax contributions. You are not restricted from making after-tax contributions when you have elected to make pre-tax contributions, as long as the total of your contributions does not exceed 10% of your compensation.

### **14) What if I want to change the percentage of my post-tax voluntary contributions?**

If you decide to make voluntary post-tax contributions and later decide to change your percentage, you must complete another form and submit it to your payroll administrator or, if you are state employee, to the Auditor's Office. Your changes will become effective as soon as the payroll administrator or the Auditor's Office processes your request.

### **15) Why can't I change my pre-tax contribution election?**

The IRS ruling provides that the pre-tax elections may not be changed as a condition of receiving this favorable tax treatment. The same condition does not apply to your after-tax elections, since you are not receiving the same favorable tax treatment on those contributions.

### **16) What is the taxable status of these contributions?**

Additional voluntary contributions made through a pre-tax election are not included in taxable income at the time the contributions are made. Also, interest earnings on your Annuity Savings Account, including interest earned from the voluntary contributions, will remain tax deferred until you receive payment via withdrawal or retirement.

If you make post-tax additional voluntary contributions instead of or in addition to pre-tax contributions, those contributions are included in taxable income when made. As with pre-tax contributions, interest earnings will remain tax deferred until you receive a refund of contributions or a retirement benefit. If you have any questions regarding the tax implications of the voluntary contributions, please consult a qualified tax advisor.

### **17) How will the voluntary contributions be invested?**

All voluntary contributions to the Annuity Savings Account will be invested in the same manner and percentage as your Annuity Savings Account monies are currently invested. You cannot separate the mandatory and voluntary contributions for investment purposes. For example, if you have all of your Annuity Savings Account invested in the Guaranteed Fund, your voluntary contributions would be invested there as well. If you have a 50%-50% split between two investment options, that same split will apply to your voluntary contributions. The election you make will automatically apply to voluntary contributions. Specific rules apply to the investment of your Annuity Savings Account. If you have questions about investments, please visit our home page on the World Wide Web at <http://www.in.gov/perf> or contact us at our toll-free number at (888) 526-1687.

### **18) How do I make voluntary contributions?**

First, you and your employer will need to complete a payroll deduction form. When you and your employer have completed the form, please submit it to PERF. The Fund will verify your earned service and whether your employer has passed a resolution opting into the program. Once the Fund makes the verification, a copy of the form will go into your file and the original will be sent to the employer for processing. The completion of the form means that you agree to have the amount you specified deducted from your take-home pay and sent to the Fund for investment.

The Fund is not responsible for any delays in the collection of contributions resulting from the improper submission of this form.

**19) How does making a contribution pre-tax or post-tax affect my take-home pay?**

With pre-tax contributions, your withholding is calculated after your contributions are deducted. With post-tax contributions, your withholding is calculated before your contributions are deducted. The difference in take-home pay can be significant. Please look at the following example:

|   |                              |                               |
|---|------------------------------|-------------------------------|
| <b><u>John Doe</u></b>                          |                              |                               |
| <b>Gross Bi-weekly Pay:</b> \$1000.00           |                              |                               |
| <b>Withholding Tax Rate:</b> 20%                |                              |                               |
| <b>Voluntary Contribution:</b> 10% of Gross Pay |                              |                               |
|   | <b>Pre-Tax Contributions</b> | <b>Post-Tax Contributions</b> |
| <b>Gross Pay</b>                                | 1,000.00                     | 1,000.00                      |
| <b>Pre-Tax Deduction</b>                        | 100.00                       |                               |
| <b>Adjusted Gross Pay</b>                       | 900.00                       | 1,000.00                      |
| <b>Withholding</b>                              | 180.00                       | 200.00                        |
| <b>Post-Tax Deduction</b>                       |                              | 100.00                        |
| <b>Net Pay</b>                                  | 720.00                       | 700.00                        |

**20) Can I make additional pre-tax voluntary contributions if I am contributing the maximum amounts to my 403(b) annuity and 457 deferred compensation plan?**

Yes. The additional pre-tax contributions (up to 10% of compensation) that you make under this program are not limited by the amounts you are contributing to your 403(b) annuity or 457 deferred compensation plan, or both. The contributions that are made under the pre-tax voluntary contribution program are not limited by section 415 of the Internal Revenue Code at the time the contributions are made to the plan; instead, they are subjected to the section 415 limits at the time you retire.

**21) Will additional pre-tax voluntary contributions to this program affect what I can contribute to my 403(b) annuity or my deferred compensation plan?**

No. The limits on your contributions to 403(b) annuities or 475 deferred compensation plans are not affected by the amount of your voluntary contributions.

**22) Can an employer withdraw from participation in the pre-tax voluntary contribution program?**

Yes, an employer may withdraw from participation in the pre-tax voluntary contribution plan at any time.

**23) What happens if my employer withdraws from participation?**

You will no longer be able to make additional contributions on a pre-tax basis. However, any funds you have already contributed will remain in your Annuity Savings Account.

**24) How should voluntary pre-tax contributions be reported on the Form W-2 issued by my employer?**

Contributions made under the pre-tax program should not be reported as taxable compensation on your Form W-2. However, if you are covered by Social Security and FICA applies to your regular wages, then the pre-tax voluntary contributions will continue to be subject to FICA taxes. Therefore, pre-tax voluntary contributions are not reported as taxable wages, but are included as "Social Security wages" on your annual Form W-2 (up to the Social Security wage base). Employers may wish to use the description "414(h)" in the "Other" box on the Form W-2 to account for the exclusion of the pre-tax voluntary contributions from income, and the inclusion of pre-tax voluntary contributions in Social Security wages.

**25) Whom can I contact with questions about voluntary contributions to my annuity savings account?**

You can contact your payroll administrator with any questions you have on starting a payroll deduction. If you are a state employee, you can contact the Auditor's Office. Increasing your Annuity Savings Account contributions could have a significant impact on your future retirement assets. If you have any questions about your Annuity Savings Account, your investment options, or the effect of these contributions, you can contact PERF for further information at 888-526-1687. You can also visit our web site at <http://www.state.in.us/perf>.

**26) Where can a member get a payroll authorization form?**

Because pre-tax voluntary contributions are tied to the employer's agreement to participate, payroll authorization forms are only available through the employer's human resources or payroll staff. They are not available from PERF.